STBB | SMITH TABATA BUCHANAN BOYES

STBB's REFERENCE GUIDE TO THE SECTIONAL TITLES SCHEMES MANAGEMENT ACT

For Managing Agents, Trustees, Owners and Property Practitioners

In this, the forty-fourth set of notes for your STSMA Reference Guide, Prescribed Management Rule 23 is discussed.

	PRESCRIBED MANAGEMENT RULE 23 – FINANCIAL MANAGEMENT - INSURANCE	REFERENCES & SEARCH WORDS
PMR 23	In a sectional title scheme, the trustees are tasked with the responsibility to arrange the "home insurance". In other words, insurance covering the bricks and mortar, the physical building (up to the median line, as well as the common property. A portion of the monthly levy contribution paid by owners is allocated to the insurance obligations of the body corporate. This insurance is obligatory and Rule 23 provides the details of the body corporate's insurance obligations. (Differentiate this from insurance for household goods kept in a unit, and the inside of the unit itself up to the median.)	Home / building insurance meaning median line definition
PMR 23(1)	The body corporate, via its trustees, are obliged to provide for insurance, because of the obligation to this effect imposed in section Section 3(1)(h) and (i).	Body corporate/trustees obligation to arrange insurance
PMR 23(1) (a)(i)	What risks are to be insured against? PMR 23(1)(a)(i) *prescribes*, as a starting point, that the risks listed in regulation 3 must be insured. These are firstly:	Risks that must be insured against (1)

	(a) lightning, explosion and smoke; (b) riot, civil commotion, strikes, lock-outs, labour disturbances or malicious persons acting in connection with any political organisation; (c) storm, tempest, windstorm, hail and flood; (d) earthquake and subsidence; (e) water escape, including bursting or overflowing of water tanks, apparatus or pipes; (f) impact by aircraft and vehicles; (g) housebreaking or any attempt thereat.	
	Secondly, trustees must adhere to instructions from its members regarding additional insurance for identified <u>risks</u>. PMR 23(1)(a)(ii) requires trustees to take out insurance for anything further in respect of which the owners passed a resolution. (See also PMR 23(8) regarding the possibility to take out additional insurance for a scheme's <u>insurable interests</u>.)	Risks that must be insured against (2) Insurable interests
	Thirdly, the trustees must insure, says PMR 23(1)(a)(iii), against any risks that banks (and other mortgagees) holding first mortgage bonds over at least 25% or more IN NUMBER of the primary sections, identify.	Risks that must be insured against (3) (mortgagees holding atleast 25% or more in number of primary sections)
	(For the sake of completeness, "primary sections" are defined in regulation 1 as "a section designed to be used for human occupation as a residence, office, shop or factory", as opposed to a "utility section" which is a section, which, in terms of by-laws, is designed to be used as an accessory to a primary section, such as a bathroom, toilet, storeroom, parking bay, parking garage, domestic worker's unit.)	'primary sections' definition
PMR 23(1)(b)	In arranging the insurance for the building, the trustees must further specify a replacement value for each unit and exclusive use area.	Replacement value for individual units and EUAs
	Any owner may give written notice to the body corporate (the trustees) and ask that the replacement value of his or her unit or exclusive use area be increased. (This will be advisable where, for example, the owner made substantial and expensive renovations to his unit.) The owner is liable for any excess payable in respect of such increase – see	Notice to increase replacement value

	PMR 23(2)(a) below.	
PMR 23(1)(c)	The trustees must ensure, when negotiating insurance cover, that the application of any ‘average clause’ to individual units and exclusive use areas is restricted. An average clause should not apply to the buildings as a whole. (What is an average clause? It becomes relevant in instances of under insurance, where your insurance cover – what your insurance policy will pay out in the case of a loss and subsequent claim - is less than what it would cost to replace the lost items. This obviously means that while your insurance payout will help you towards replacing your losses, you will have to partially fund this replacement. In other words, there is a shortfall between the amount of cover selected and the actual replacement value of what is being insured. The result is that you will only be paid a proportional part of your claim, by virtue of the application of the principle of ‘averaging’.) What is the aim of this PMR? It means that the ‘average clause’ calculation that is applied if the units (only) are under insured may not apply to the common property (and buildings beyond the median line including all improvements e.g. swimming pools etc, if these items appear to be under insured. Trustees must ensure that the above requirement has been met in the policy, otherwise they may be found to have acted negligently.	Restriction on ‘average clauses’ ‘average clause’ definition
PMR 23(1)(d)	The insurance policy must further include a clause generally allowing any bondholder (over a section or exclusive use area) to enforce the terms of the insurance policy. This may seem odd at first glance, but it is a standard requirement from banks when granting bonds, to make sure that the property that is being bonded is indeed repaired to the extent provided for in an existing insurance policy, should the body corporate fail to do so.	Ceding rights to claim under the insurance policy to a mortgagee / mortgagee enforcement of policy terms

PMR 23(1)(d)	The policy may include provision for payment of "excess" amounts. This is practically of huge importance because, when units are closely joined together, as is the case in many sectional title schemes, there is always a danger that a mishap in one unit, e.g. a serious water leak, a bursting geyser or a gas explosion, will affect other units. The body corporate's insurance will cover such incidents and owners are protected. However, if the problem originates in an owner's unit and spreads to areas of the common property, the owner will have to pay the excess on the insurance claim instituted by the body corporate. On the other hand, if the problem originates in the common property, e.g. on the roof, the body corporate will be liable for the excess payment. See PMR 23(2)(2) below.	'Excess' payments Who pays excess depending on where problem originates
PMR 23(2)	An owner is responsible for: 1. Payment of any additional premium payable if an increase in the insured value of the unit is requested by that owner – see PMR 23(1)(b). 2. Any excess amount that relates to damage to any part of the common property (including the part of the buildings outside the median line) inasfar as it arises from a failure to properly repair and maintain his unit and exclusive use area. Such owner must within 7 days after being requested by the body corporate to do so, furnish the latter with proof of payment of the excess by the owner's insurer.	Owner liability for increase in value of unit and excess amounts
PMR 23(3)	To ensure insurance policies remain updated with increases (and decreases) in the value of the common property in the scheme insured, the trustees must, on behalf of the body corporate, obtain a replacement valuation of all buildings and improvements at least every three years. This valuation must be presented to all body corporate members at the AGM.	Replacement values every three years, AGM

PMR 23(4)	At the AGM, in addition to the updated schedules referred to in PMR 23(3), the trustees must prepare schedules showing estimates of- (a) the replacement value of the buildings and all improvements to the common property; and (b) the replacement value of each unit, the total value of all units – which must be equal to the estimated replacement values referred to in (a).	Schedules of values for AGM
PMR 23(5)	On written request by any registered bondholder (and the furnishing of satisfactory proof), the trustees must record the cession to that bondholder of that member's interest in any of the proceeds of the insurance policies of the body corporate.	Recording of cession to a mortgagee
PMR 23(6)	Public liability cover is obligatory. PMR 23(6) obliges a body corporate's trustees also to take out public liability insurance to cover the risk of any liability it may incur in respect of injury, death or illness on or in connection with the common property; and any damage / loss of property as a result of an occurrence or happening in connection with the common property. The owners will determine the amount of such cover in a general meeting, usually the AGM, but it may not be less than R 10 million.	Risks that must be insured against (4) Obligatory public liability cover
PMR 23(7)	Note further that fidelity insurance (i.e. insurance against damage or loss arising from any act of fraud or dishonesty committed by a trustee, managing agent, employee or other agent of the body corporate) is obligatory. PMR 23(7) obliges a body corporate to ensure that such insurance cover is in place.	Risks that must be insured against (5) Obligatory fidelity insurance cover

	The amount of the insurance is to be determined by the owners in a general meeting, which will usually be the AGM.	
PMR 23(8)	Owners may, by special resolution, direct the trustees to take out additional insurance, apart from the items prescribed in this Rule in respect of insurable interests relating to the land and buildings forming part of the common property (for example a frail care facility or a generator, or to insure against risks that the body corporate fails in its functions).	Risks that must be insured against (6) Special resolution: insurable interests

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